

August 14, 2006
Members of the Investment Committee
California Public Employees' Retirement System
Lincoln Plaza East
400 Q Street, Suite E4800
Sacramento, CA 94814

Re: International Public Real Estate Equity Securities Request for Proposal - Finalists

Dear Members of the Investment Committee:

Pension Consulting Alliance, Inc. ("PCA") was requested by CalPERS Staff to assist with the Request for Proposal No. 2005-3831 ("RFP") for International Public Real Estate Equity Securities ("PREES") Management – Spring-Fed Pool. PCA served on the Evaluation Committee in a non-voting capacity; and specifically, our scope of work involved reviewing and commenting on respondent proposals, participating in respondent interviews and conducting onsite visits to the finalists' offices.

Staff has completed the evaluation process and they are recommending approval of the following five managers for the Spring-Fed Pool, subject to completion of final due diligence and successful negotiation of terms and conditions (listed in no particular order):

- 1) Citigroup Property Investors
- 2) European Investors Incorporated
- 3) Morgan Stanley Investment Management
- 4) PRESIMA Inc
- 5) RREEF America LLC.

PCA's assessment of each finalist is as follows:

Citigroup Property Investors

Citigroup Property Investors ("Citigroup") uses a detailed bottom-up valuation model to select and manage its international PREES strategy. This in-depth bottom-up model includes a discounted cash flow analysis and an implied NAV calculation. Citigroup completes a discounted cash flow and NAV model for each stock in the investible universe and updates them regularly. Citigroup's management team uses its detailed bottom-up analysis to build a diversified portfolio that includes 50 to 70 international stocks that has historically averaged 30% to 50% annual turnover.

Citigroup's international PREES management team was recently formed in 2004. As such, Citigroup has limited experience working together and a limited track record managing an international PREES strategy. The current management team includes six dedicated investment professionals, two of which are located outside the U.S in Citigroup's London office. The small team size requires each investment professional to track a large number of stocks. Given the level of detailed analysis Citigroup completes on each stock, it may become difficult for the current management team to adequately cover the growing international PREES universe. Citigroup intends to expand its management team by adding an office in Asia. The two analysts located in the London office are currently covering the Asia region.

European Investors Incorporated

European Investors Incorporated (“European Investors”) has a successful track record investing in international PREES since 2000. The strategy implemented by European Investors is characterized by low annual turnover, which has averaged approximately 20% since inception, and holdings concentration of between 30 to 40 stocks internationally. The low turnover and concentrated number of holdings demonstrates the investment conviction of European Investors’ management team. They identify potential stocks for investment by completing an in-depth valuation of each stock that includes a discounted cash flow analysis, dividend discount model, and an implied NAV calculation.

European Investors’ management team includes six investment analysts and two portfolio managers. Two of the team members are located in New York, four in Amsterdam, and two in Singapore. However, the office in Singapore was recently established and its two team members, although experienced, are relatively new additions to the firm. The lead portfolio manager, Mr. Jim Rehlaender, oversees the international PREES strategy and is a key man in the successful implementation of the strategy. Should Mr. Rehlaender no longer be a substantial part of the team, the strategy could suffer.

Morgan Stanley Investment Management

Morgan Stanley Investment Management (“Morgan Stanley”) has one of the longest and most successful track records investing in international PREES. Morgan Stanley has been investing in PREES in Europe and Asia since 1997. Additionally, each portfolio manager has a minimum of nine years experience in international PREES and has equal tenure in their present roles at Morgan Stanley. Morgan Stanley’s team is located in each region in which the international PREES strategy invests. There are three offices which are located in New York, London, and Singapore. Morgan Stanley invests in approximately 30 to 40 stocks within each region and has average annual historical turnover of 30% to 50%.

Morgan Stanley’s management team consists of six dedicated investment professionals. The relatively small team size requires each investment professional to track a large quantity of stocks. Going forward, the team may have to expand to sufficiently track the growing number of international PREES. Mr. Ted Bigman leads the management team. Mr. Bigman directs the international PREES strategy and oversees the asset allocation framework across the regions. As such, Mr. Bigman is a key man in the successful implementation of the international PREES strategy. Should Mr. Bigman no longer spend a significant portion of his time on the international PREES strategy, the successful management of the strategy may be compromised.

Presima Inc.

Presima Inc. (“Presima”) has been successfully implementing an international PREES strategy since 1998 as an internal investment manager for the Caisse de dépôt, the largest Canadian institutional investor. Now, Presima is offering its investment management expertise to outside investors. Presima’s implements a concentrated strategy with 30 to 35 international stocks and has high average annual turnover of over 100% historically. Presima seeks to capitalize on all inefficiencies presented within the international PREES market and as such experiences higher annual turnover.

The management team is located in Montreal, Canada. The team is comprised of nine dedicated investment professionals that have extensive experience working together for the Caisse de dépôt. However, it may be more difficult to stay abreast of international market trends and stocks from its Canada location, especially as the international PREES universe grows.

RREEF

RREEF has one of the largest dedicated international PREES management teams, consisting of thirteen investment professionals. The management team was recently formed in 2004. However, the portfolio managers hired by RREEF have extensive PREES experience investing within their respective regions (Europe and Asia). RREEF manages its international PREES strategy through regional mandates, in which each regional portfolio manager is responsible for stock selection within their respective regions. This investment process fully utilizes the regional experience of the individual team members. The international PREES team members are located in Chicago, London, Hong Kong, and Sydney. RREEF's team implements a diversified core strategy that holds between 80 and 90 international stocks with average annual turnover of 50% to 65% historically.

Due to the recent formation of the team, RREEF has a limited track record investing in international PREES. As such, the team and strategy are somewhat untested.

Recommendation

The five finalists selected by CalPERS' Staff appear to have the ability to successfully manage international PREES portfolios. However, as described above, the characteristics of each manager varies by strategy, track record, experience and tenure of the management teams. PCA concurs with CalPERS' Staff's recommendation of the five finalists, but suggests that the commitment amounts to be allocated by CalPERS should be based on the relative qualifications of the five selected firms.

We look forward to answering any questions at the Investment Committee meeting in August.

Very truly yours,



Nori Gerardo Lietz
Managing Director

Cc: Russell Read
Anne Stausboll
Al Fernandez
Judy Alexander
Jane Delfendahl
Pam Alsterlind
Eliza Bailey